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O F F I C E O F N A T I O N A L E S T I M A T E S

25 October 1957

STAFF MEMORANDUM 49-57

SUBJECT: The Spanish Situation

1. The last Spanish estimate, NIE 27.1-56, 12 June 1956 stated that "we believe that the present regime will be able to remain in power for at least several more years, assuming Franco . . . remains active." Eight months later, our memorandum to the DCI of 27 February 1957 pointed out that Franco's position had been progressively weakened by deteriorating economic conditions, bolder popular opposition, and increasing factionalism within the government. We then altered our opinion to state that ". . . Franco will be able to control the situation for at least two more years." Now, however, developments in Spain indicate that the threat to Franco's position could be of a more immediate and serious nature than the above estimates suggest. This memorandum is designed as an interim assessment of that threat pending production of a new Spanish NIE, scheduled for next March. *(Signature)*

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2. The Economic Problem. There has been a continued deterioration of the Spanish economic situation during the year, with unchecked inflationary pressures threatening to become critical. Exceptionally bad weather in recent years has been a major contributor to these economic difficulties. In particular, 1955-56 crop failures have reduced exports, necessitated sizeable agricultural imports, and pushed prices upward. However, the rise in inflationary pressures is mainly due to the expansion of economic activity -- industrial production currently has increased about 50 percent over the 1951 figure -- stimulated by the government and to a somewhat lesser extent by the \$400-500 million US air base construction program. Because of Spain's lack of investment capital, business expansion and public development have been financed largely through inflationary means. Governmental expenditures exceed revenues by about 30 percent. Bank credit has been increasingly extended, and money supply was expanded by over 20 percent last year.

3. The rate of increase in the cost-of-living index is picking up speed; it rose seven percent in 1955 and 10 percent last year (based on official prices; the actual increase may have been as much as 50 percent during the two years). In an attempt to adjust private incomes

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to soaring living costs, the regime raised wages and social security benefits by about 40 percent in 1956. But these wage increases now seem to have been fully absorbed by the continuous price rise since last November. Labor dissatisfaction and unrest have been greatly stimulated by this inflationary squeeze, creating a major element of tension in the Spanish scene.

4. The external implications of inflation are equally serious, with the balance of payments deficit rising sharply and dollar reserves declining rapidly. Official gold reserves have remained unchanged at \$120 million. However, in view of the 1956 trade deficit on visible account of over \$300 million, the regime was forced to draw down dollar reserves. Despite US aid deliveries of about \$218 million last year, dollar holdings declined \$61 million in 1956 and by a further \$18 million during the first quarter of 1957 -- to a level of \$14 million. US aid commitments of approximately the same magnitude for FY 1958, plus a somewhat better agricultural outlook, suggest that the regime might stem the tide of foreign exchange losses. But any real improvement in the situation will depend on the government's willingness and ability to reduce deficit financing, restrict imports, and stabilize wages and prices. To take any or all of these measures will require

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major decisions. Yet basic divisions within the ruling coalition limit the regime's ability to make such decisions without alienating large groups of its supporters.

5. The Political Problem. While the economic situation provides a ready catalyst for opposition to the regime, the more fundamental problem is that Franco's formula for governing Spain appears in danger of breaking down after more than a decade of fitful survival. Time and changing conditions have greatly reduced Franco's ability to trade on Spanish fears of civil strife. At age 65, his political future is limited, but so far he has refused to risk his monopoly of power by formally providing a solution to the succession issue. Hence, government factions are already jockeying for power in anticipation -- both hopeful and fearful -- that his death will occur before that issue is resolved. The regime's somewhat superficial unity thus is being increasingly diminished by severe factional disputes, especially over approaches to economic problems.

6. Any open conflict within the regime would be most likely to pit the Falange Party against the traditional landed and financial interests. Both groups are bent on establishing political hegemony;

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the issues separating them leave little room for compromise; and events are moving in a direction likely to broaden the cleavage between them. Although still pulled in different directions by its own internal conflicts, the Falange now appears to be stressing anti-capitalist and anti-monarchical themes in an effort to win acceptance among urban labor. It will probably support and might lead workers demands for wage increases during the next few months. Moreover, there may be a considerable increase in its influence in the labor field as a result of recent legislation favoring Falange syndicalist activity.

7. There are also signs of some reduction of support for Franco within two powerful groups -- the Army and the Church -- which hitherto have been his staunchest supporters. Although Franco still retains control of the Army -- especially through its top officers -- there are reports of discontent among the lower and middle-grade officers. The Catholic Church hierarchy, while showing somewhat greater concern for the Spanish poorer classes than in the past, remains generally committed to support the regime. But an increasing segment of the clergy fears that, in the event of serious anti-regime disorders, the Church's past close collaboration with Franco will expose it to violent anti-clericalism.

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8. Short-Term Prospects. The fact remains that opposition to the Franco regime, although deep-seated and widespread, is still largely incoherent and leaderless. The regime could probably control any student and labor protest demonstrations which are likely to take place in the immediate future, unless these should unexpectedly take on a violent and epidemic character. However, events are moving in a direction inimical to Franco's traditional methods of rule, and this trend is gaining sufficient momentum to cause us to be less confident that "Franco will be able to control the situation for at least two more years."

9. In the short term, the acuteness of the economic problems probably will provide the key to the scope and intensity of any agitation against the government. There is at least an even chance that Franco either will refuse to take the necessary drastic measures or will be able to at least temporarily postpone them by a combination of: (a) a favorable agricultural outlook, (b) continued US aid of at least present proportions, and (c) some success with moderate measures. If he could avoid a major decision, Franco would gain time to cope with his political problems, probably by continuing his penchant for playing one faction off against the other. In that case it is unlikely that there would be disorders of a sufficient magnitude to pose a significant threat to the

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regime during the next six months or so. The basic problems nevertheless would remain unsolved. Further, there is a danger that by postponing more effective economic decisions, the situation might get out of hand. If deterioration of the economy should approach the point of an economic collapse, public disorder and political disaffection might force Franco to adopt a strong economic program and to resort to repressive military government in order to carry it out.

10. We believe that Franco would turn to the army only if he were ready to admit the bankruptcy of his regime, and therefore that he will be driven to adopt far-reaching economic measures before a collapse of the economy occurs. However, if he supports a program of austerity, including wage stabilization and reduced public expenditure, labor will almost certainly protest. If these measures were taken against a background of rapidly deteriorating economic conditions the labor reaction would probably be violent. On the other hand, if Franco grants sizeable wage increases with strict controls on prices, he will jeopardize his position with conservative elements who have been his principal supporters. In either case, he would stimulate labor and the conservatives to seek alternative regimes more in line with their particular interests. In this way, he might be forced to call upon the army and thus open the door to civil conflict or to a military dictatorship in which he might be swept aside along with the paraphernalia of his regime.

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11. In sum, the present fluid situation in Spain constitutes the most serious challenge Franco has faced in years, and will require masterful use of his dwindling resources. We do not believe that his regime is immediately threatened or that such a threat will arise over the next several months, even though a degree of public disorder is likely. Indeed, there is at least an even chance that Franco for a considerable period will be able to avoid taking actions which might put his control of the country in jeopardy. However, we also believe that his political, and perhaps his economic, difficulties are likely to increase rather than diminish with time. The evidence is not yet sufficient to provoke a reversal of our previous estimates, but it does diminish the degree of assurance with which we hold to them. The major imponderable in this situation is the temper of the Spanish population; it has shown great capacity to endure privations, but its aspirations have been reawakened and it has demonstrated in the past a great capacity for bloody revolution and reprisal.

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